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IN THE

Supreme Court of the United States

OCTOBER TERM, 1993

NCR CORPORATION,
Petitioner,

v.

TAXATION AND REVENUE DEPARTMENT
OF THE STATE OF NEW MEXICO,
Respondent.

On Petition for a Writ of Certiorari to the Court of Appeals of New Mexico

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BRIEF OF AMICUS CURIAE TAX EXECUTIVES INSTITUTE, INC. IN SUPPORT OF PETITIONER

TIMOTHY J. MCCORMALLY
Counsel of Record
MARY L. FAHEY
TAX EXECUTIVES INSTITUTE, INC.
1001 Pennsylvania Ave., N.W.
Suite 320
Washington, D.C. 20004-2505
(202) 638-5601
Counsel for Amicus Curiae
Tax Executives Institute, Inc.

WILSON - EPES PRINTING CO., INC. - 789-0096 - WASHINGTON, D.C. 20001

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BRIEF OF AMICUS CURIAE TAX EXECUTIVES INSTITUTE, INC. IN SUPPORT OF PETITIONER

INTEREST OF AMICUS CURIAE

Pursuant to Rule 37 of the Rules of this Court, Tax Executives Institute, Inc. respectfully submits this brief as *amicus curiae* in support of the petitioner.[1] Tax Executives Institute (hereinafter "TEI" or "the Institute") is a voluntary, non-profit association of corporate and other

[1] TEI has requested and received the written consents of the Petitioner and the Respondent to the filing of this brief; those consents have been filed with the Clerk of this Court.

business executives, managers, and administrators who are responsible for the tax affairs of their employers. The Institute was organized in 1944 and has approximately 4,900 members who represent more than 2,400 of the leading corporations in the United States and Canada.

TEI is dedicated to promoting the uniform and equitable enforcement of the tax laws throughout the Nation, to reducing the costs and burdens of administration and compliance to the benefit of both the government and taxpayers, and to vindicating the Commerce Clause and other constitutional rights of all business taxpayers. The members of the Institute represent a cross-section of the business community in North America and are, almost without exception, engaged in interstate or foreign commerce. The multijurisdictional companies represented by the Institute's membership are significantly affected by the allocation and apportionment of income among the various States. As a result, TEI's members will be directly affected by the Supreme Court's decision whether to grant a writ of certiorari in this case.

The issue presented in this case is whether New Mexico and other States are precluded from taxing foreign-source dividends, interest, and royalties that have already been subject to tax on an unapportioned (*i.e.*, allocated) basis by foreign countries and, if so, on what basis such taxation may occur. The case raises fundamental issues about the rights embodied in the Foreign Commerce Clause of the Constitution and the legitimacy of a State's apportionment scheme under the Interstate Commerce and Due Process Clauses. *Amicus* TEI submits that a writ of certiorari should be issued here to enable the Court to confirm that the Commerce and Due Process Clauses do not permit apportionment without taking into account the apportionment factors of the business generating that income and, further, that the Foreign Commerce Clause

proscribes the taxing of foreign-source income that is already subject to tax on an unapportioned basis by foreign countries.

There can be no doubt that this case raises a recurring issue having a broad effect on U.S. companies operating overseas and receiving dividends, interest, and royalties from overseas affiliates. The amount of dividends alone paid or constructively received by domestic corporations from foreign sources in 1986 totalled over $22 billion.[2] Because TEI members and the companies by whom they are employed will be materially affected by the Court's decision, the Institute has a special interest in the outcome of this case.

SUMMARY OF ARGUMENT

1. Under the Commerce and Due Process Clauses of the Constitution, a State may not tax value outside its borders. Such taxation is proscribed because the "fundamental purpose of the [Commerce] Clause is to assure that there be free trade among the several States," *Boston Stock Exch. v. State Tax Comm'n*, 429 U.S. 318, 335 (1977), and because extraterritorial taxation offends fundamental notions of due process and constitutes an "unreasonable clog upon the mobility of commerce." *Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511, 527 (1935).

This Court has rightly observed that dividing income among the several States bears some resemblance to "slicing a shadow." *Container Corp. v. Franchise Tax Board*, 463 U.S. 159, 192 (1983). A reasonable balance must be struck between the State's legitimate need for revenue and the taxpayer's legitimate right to protection from overreaching taxing authorities. To pass constitutional muster, the apportionment formula must be fair: It must

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[2] Karla M. Daronco, *1986 Corporation Foreign Tax Credit, A Geographic Focus*, 10 STATISTICS OF INCOME BULL. 31, 46 (IRS Pub. No. 1136, Winter 1990-91).

be marked by both internal and external consistency. *Container Corp.*, 463 U.S. at 169.

Here, the issue is whether the apportionment formula used by New Mexico is properly designed to ensure against the proscribed taxation of extraterritorial values. In this case, the State of New Mexico included all of NCR Corporation's dividends, interest, and royalties from its foreign subsidiaries in its apportionable tax base, even though that income was subject to tax on an allocated (or unapportioned) basis in the foreign countries where NCR Corporation does business. Moreover, the State refused to include in the denominator of the three-factor apportionment formula the property, payroll, and sales that produced that income.

Amicus TEI submits that an apportionment formula that fails by design to take into account the factors generating the apportioned income is constitutionally flawed. Thirteen years ago, the Court acknowledged that the factor representation issue could be one of constitutional import, but declined to resolve it on the ground that the issue had not been properly raised by the taxpayer. *Mobil Oil Corp. v. Commissioner of Taxes*, 445 U.S. 425, 441 n.15 (1980). Justice Stevens, however, found the issue dispositive and would have proscribed "lump[ing] huge quantities of investment income that have no special connection with the taxpayer's operations in the taxing State into the tax base" without taking into account the factors that produced that income. *Id.* at 461 (Stevens, J., dissenting).

Without a doubt, New Mexico's apportionment formula should be struck down as violating *Container Corp.*'s requirement of fairness: It is internally inconsistent in that if it were applied by every jurisdiction it would result in more than 100 percent of NCR Corporation's income being taxed, and it is externally inconsistent in that it does not represent a reasonable sense of how the income

was generated. Only by requiring factor representation can the Court vindicate the constitutional requirement of a "fair" apportionment formula.

2. The constitutional prohibition against state taxation of *foreign* commerce is "broader than the protection afforded to interstate commerce . . . ." *Kraft Gen. Foods, Inc. v. Iowa Dep't of Revenue & Finance,* 112 S. Ct. 2365, 2370 (1992). *Amicus* TEI submits that, even if New Mexico's statute does not offend the Interstate Commerce and Due Process Clauses, it must fall under the Foreign Commerce Clause.

To prevent multiple taxation of interstate commerce, a State's apportionment formula must be applied in a manner such that "no instrumentality of commerce is subjected to more than one tax on its full value." *Japan Line, Ltd. v. County of Los Angeles,* 441 U.S. 434, 447 (1979). If a State's taxing scheme "inevitably" leads to multiple taxation, it must be struck down under the Foreign Commerce Clause. *Container Corp.*, 463 U.S. at 188; *Japan Line,* 441 U.S. at 447.

In this case, the State of New Mexico included in the apportionable tax base the dividends, interest, and royalties received by the taxpayer from its foreign subsidiaries —income that was subject to tax in full without apportionment by foreign taxing authorities. If other States were to follow New Mexico's lead, "various instrumentalities of commerce could be subjected to varying degrees of multiple taxation, a result that would plainly prevent this Nation from 'speak[ing] with one voice' in regulating commerce." *Japan Line,* 441 U.S. at 450-51 (quoting *Michelin Tire Corp. v. Wages,* 423 U.S. 276, 285 (1976)).

Amicus TEI submits that the Foreign Commerce Clause does not permit such apportionment of foreign income without taking into account the property, payroll, and sales factors that generated the income. The Court should

grant a writ of certiorari to address the question left open in *Mobil*.

3. A writ of certiorari should also issue in this case because the decision of the New Mexico Court of Appeals conflicts with this Court's 1992 decision in *Kraft General Foods*. In that case, the Court found that the State's preference for domestic commerce (which was evidenced by permitting a deduction for dividends received from domestic, but not foreign subsidiaries) over foreign commerce was inconsistent with the Constitution. The Court therefore invalidated the Iowa statute because it "facially discriminate[d] against foreign commerce and therefore violate[d] the Foreign Commerce Clause . . . ." 112 S. Ct. at 2372.

Like the Iowa statute involved in *Kraft General Foods*, the New Mexico statute here defines "net income" as federal taxable income with certain adjustments for New Mexico tax purposes. Because NCR Corporation filed returns on a federal consolidated basis, transactions between members of the domestic consolidated group (such as dividends, interest, and royalties) were effectively eliminated from NCR Corporation's apportionable base for New Mexico tax purposes. Thus, under the New Mexico statute, NCR Corporation's taxable income did not generally include dividends, interest, and royalties received from domestic subsidiaries, but did include similar intercompany payments received from its foreign subsidiaries. Moreover, the factors that generated that income from the domestic subsidiaries were included in NCR Corporation's apportionable tax base, whereas the factors relating to the foreign subsidiary income were not.

In *Kraft General Foods*, the Court found the dichotomy between the treatment of dividends received from domestic and foreign subsidiaries discriminatory, unjustified, and constitutionally fatal. *Id.* at 2372. *Amicus* TEI sub-

mits that the New Mexico statute is similarly flawed. *See also Boston Stock Exch.*, 429 U.S. at 329, where the Court unequivocally held that the Commerce Clause proscribes the granting of a preference to one form of commerce over another. This Court should grant certiorari to reject this preference.

ARGUMENT

I. NEW MEXICO'S FAILURE TO PROVIDE FACTOR REPRESENTATION VIOLATES THE COMMERCE AND DUE PROCESS CLAUSES

Under the Commerce and Due Process Clauses of the Constitution,[3] a State may not tax value outside its borders. *E.g., Connecticut Gen. Life Ins. Co. v. Johnson*, 303 U.S. 77, 80-81 (1938). Such taxation is proscribed because the "fundamental purpose of the [Commerce] Clause is to assure that there be free trade among the several States," *Boston Stock Exch. v. State Tax Comm'n*, 429 U.S. 318, 335 (1977), and because extraterritorial taxation offends fundamental notions of due process and constitutes an "unreasonable clog upon the mobility of commerce." *Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511, 527 (1935).

This Court has rightly observed that dividing income among the several States bears some resemblance to "slicing a shadow." *Container Corp. v. Franchise Tax Board*, 463 U.S. 159, 192 (1983).[4] Absolute consistency, even

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[3] U.S. Const. art. I, § 8, cl. 3 (Commerce Clause); U.S. Const. amend. XIV, § 1 (Due Process Clause).

[4] Although the terms "allocation" and "apportionment" are often used interchangeably in respect of the division of income among various jurisdictions, "allocation" properly refers to the "attribution of a particular type of income or receipt or property or the like to a designated State, [and] 'apportionment' refers to the division of the tax base by formula." JEROME R. HELLERSTEIN & WALTER HELLERSTEIN, STATE TAXATION I: CORPORATE INCOME AND FRANCHISE TAXES ¶ 9.01, at 9-5 n.1 (2d ed. 1993). A typical "three-factor" formula—similar to the one used by the State of New Mexico

among taxing authorities using the same apportionment formula, "may just be too much to ask," *id.*,[5] but there are constitutional limits on a State's use of an apportionment formula, especially in respect of income derived in foreign commerce.[6] In other words, a balance must be struck between the State's unmistaken need for revenue and the taxpayer's legitimate right to protection from overreaching taxing authorities. It is for this Court to ensure that the balance is a reasonable one.[7] If the State

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in this case—compares (i) the taxpayer's property, payroll, and sales (receipts) within the taxing State to (ii) the taxpayer's total property, payroll, and sales. UNIFORM DIVISION OF INCOME FOR TAX PURPOSES ACT (U.L.A.), §§ 9-15. Some jurisdictions use single-factor, double-factor, or weighted-factor formulae. HELLERSTEIN & HELLERSTEIN, *supra*, at ¶ 9.06.

[5] Although an apportionment formula may be "imperfect," it is nevertheless an "acceptable method of measuring the in-state earnings of an integrated business." *Mobil Oil Corp. v. Commissioner of Taxes*, 445 U.S. 425, 452 (1980) (Stevens, J., dissenting). One means of taxing in-state income is the use of the unitary business principle which calculates the local tax base by first defining the scope of the unitary business of which the taxed enterprise's activities in the taxing jurisdiction form one part, and then apportioning the total income of the unitary business between the taxing jurisdiction and the rest of the world based on a formula taking into account objective measures of the corporation's activities within and without the jurisdiction. *Container Corp.*, 463 U.S. at 165. The apportionment system used by the State of New Mexico is based on the unitary business principle. Appendix B to NCR Corporation's Petition for a Writ of Certiorari to the Court of Appeals of New Mexico (App.), at 41a-42a (No. 93-541).

[6] In evaluating challenges to state taxing schemes, the Court examines the practical effect of a challenged tax to determine whether it "is applied to an activity with a substantial nexus with the taxing State, is fairly apportioned, does not discriminate against interstate commerce, and is fairly related to the services provided by the State." *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977).

[7] *See Boston Stock Exch.*, 429 U.S. at 329 (the Court has a duty "to make the delicate adjustment between the national interest in free and open trade and the legitimate interest of the individual States in exercising their taxing powers").

has not "given anything for which it can ask return" in respect of the person, property, or transaction it seeks to tax, *Wisconsin v. J.C. Penney Co.*, 311 U.S. 435, 444 (1940), the Commerce and Due Process Clauses operate as a constitutional brake upon the State's raw power to tax.

To pass constitutional muster under the Commerce and Due Process Clauses, the apportionment formula must, first and foremost, be fair. *Container Corp.*, 463 U.S. at 169. There must be internal consistency: "[T]he formula must be such that, if applied by every jurisdiction, it would result in no more than all of the unitary business' income being taxed." *Id.* There must also be external consistency: "[T]he factor or factors used in the apportionment formula must actually reflect a reasonable sense of how income is generated." *Id.*

Here, the issue is whether the apportionment formula used by New Mexico is properly designed to ensure against the proscribed taxation of extraterritorial values. In this case, the State of New Mexico included all of NCR Corporation's dividends, interest, and royalties from its foreign subsidiaries in its apportionable tax base, even though the income was subject to tax on an allocated (or unapportioned) basis in the foreign countries where NCR Corporation does business. (App. B at 25a-26a.) Moreover, the State refused to include in the denominator of the three-factor apportionment formula the property, payroll, and sales that produced that income.[8] Thus, New

[8] The parties stipulated that the gross amount of the payments received by NCR Corporation in the form of dividends, royalties, and interest was gross income earned directly by NCR Corporation. Consequently, NCR Corporation was subject to the taxing jurisdiction of each of the host countries in respect of this income. The tax on the income was generally paid through a withholding mechanism that required the subsidiary to withhold tax on the payment at a flat rate and pay over the amount of NCR Corporation's tax liability to the foreign country. The withholding rates ranged from 0 percent to 40 percent of the gross amount. (App. B at 25a-26a.)

Mexico's taxing scheme did not provide for "factor representation" in respect of NCR Corporation's foreign income.

Amicus TEI submits that an apportionment formula that fails by design to take into account the factors that generated the apportioned income is constitutionally flawed because there can never be a "rational relationship between the income attributed to the State and the intrastate values of the enterprise." *Mobil*, 445 U.S. at 436-37. The failure to provide factor representation is "inherently arbitrary," *Underwood Typewriter Co. v. Chamberlain*, 254 U.S. 113, 121 (1920), and cannot help but produce a result that reflects neither "a reasonable sense of how [the] income [was] generated" (as required by *Container Corp.*, 463 U.S. at 169) nor "the relative contribution of the activities in the various States [specifically, New Mexico] to the production of total unitary income" (*Butler Bros. v. McColgan*, 315 U.S. 501, 509 (1942)).[9] This Court's prior holdings teach this conclusion and common sense confirms it.

In *Mobil*, the Court acknowledged that the factor representation issue could be one of constitutional import, but declined to resolve it on the ground that the issue had not been properly raised by the taxpayer. 445 U.S. at 434, 441 n.15, 449.[10] Justice Stevens, however, found

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[9] The skewed manner in which the State of New Mexico applies its apportionment formula is readily apparent when one considers that the State seeks to include the foreign-source income in the calculation, but "refuses to go any further in recognizing the unitary principle" by including the apportionment factors. *See American Tel. & Tel. Co. v. Wisconsin Dep't of Revenue*, 422 N.W.2d 629, 632 (Wis. App. 1988).

[10] The lower court's statement in this case (App. A at 16a) notwithstanding, the Court did *not* reject the concept of factor representation in *Mobil*. Rather, the Court reserved the question, stating that "we need not, and do not, decide whether combined apportionment of this type [inclusion of the Mobil subsidiaries' and affiliates' sales, payroll, and property in the apportionment formula]

the issue dispositive and would have proscribed "lump-[ing] huge quantities of investment income that have no special connection with the taxpayer's operations in the taxing State into the tax base" without taking into account the factors that produced that income. 445 U.S. at 461 (Stevens, J., dissenting). Justice Stevens explained:

> Unless the sales, payroll, and property values connected with the production of income by the payor corporations are added to the denominator of the apportionment formula, the inclusion of earnings attributable to those corporations in the apportionable tax base will *inevitably* cause Mobil's Vermont income to be overstated.

Id. (emphasis added). *See also* JEROME R. HELLERSTEIN & WALTER HELLERSTEIN, STATE TAXATION I: CORPORATE INCOME AND FRANCHISE TAXES ¶ 9.13[3][b], at 9-87 (2d ed. 1993) (if the unitary concept is the foundation for the inclusion of dividends in the apportionable base, that concept "should carry through to all aspects of the tax computation," including factor representation).

In a 1991 case, the Maine Supreme Court forthrightly addressed this issue and held that the lack of factor representation was constitutionally fatal to a taxing scheme:

> [Without factor representation,] [t]he ineluctable result is that more of the business activity of the unitary business is attributed to [the State] than is the actual case. Thus, the income taxable by [the State] under the Assessor's formula does not truly reflect [the corporation's] connection with [the State] and

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is constitutionally required." 445 U.S. at 441 n.15. *See also id.* at 449 ("[b]ecause the issue has not been presented, we need not, and do not, decide what the constitutent elements of a fair apportionment formula applicable to such income would be"). The reservation of this issue was specifically recognized by the Court in *Container Corp.*, 463 U.S. at 168 n.5, and by the hearing officer in this case, App. B at 54a.

> fails to meet the test of fairness required by the due process clause.

Tambrands, Inc. v. State Tax Assessor, 595 A.2d 1039, 1044 (Me. 1991).[11]

The compelling nature of Justice Stevens's reasoning is illustrated by the following example. Assume that the taxpayer's activities within the United States are conducted exclusively in New Mexico—that is to say, 100 percent of its domestic property, payroll, and sales are in that State. Assume further that the taxpayer owns a foreign subsidiary whose property, payroll, and sales are equal to the taxpayer's U.S. (New Mexico) factors. Finally, assume that the taxpayer makes $100 from its New Mexico operations and receives a $100 dividend from its foreign subsidiary (which dividend is subject to a withholding tax by the foreign country). Under New Mexico's taxing scheme, all of the taxpayer's income would be apportioned to New Mexico. Thus, 100 percent of the foreign

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[11] In addition to Maine, other States have concluded that the failure to provide factor representation in applying the apportionment rules to unitary businesses contravenes the Due Process and Commerce Clauses. *See, e.g., American Tel. & Tel. Co. v. Wisconsin Dep't of Revenue*, 422 N.W.2d at 636 (involving dividends from unitary subsidiaries); *Homart Dev. Co. v. Norberg*, 529 A.2d 115, 121 (R.I. 1987) (involving distributive share from partnership). *See also NCR Corp. v. South Carolina Tax Comm'n*, 402 S.E.2d 666, 674 (S.C. 1991) (case remanded to determine appropriate factors to include with respect to interest and royalties from unitary subsidiaries); *NCR Corp. v. Comptroller of Treasury*, 544 A.2d 764, 781 (Md. 1988) (same with respect to dividends from unitary subsidiaries). *See* E. George Rudolph, *State Taxation of Interstate Business: The Unitary Business Concept and Affiliated Corporate Group*, 25 TAX L. REV. 171, 205 (1970) ("Obviously, if the foreign source income is included in the base for apportionment, foreign property, payrolls, and sales must be included in the apportionment fractions. This was recognized in *Bass* [, *Ratcliff & Gretton, Ltd. v. State Tax Comm'n*, 266 U.S. 271 (1924)] . . ."). *But see NCR Corp. v. Commissioner of Revenue*, 438 N.W.2d 86, 94 (Minn.), *cert. denied*, 493 U.S. 848 (1989) (excluding foreign subsidiaries' factors does not result in constitutional violation).

dividend would be apportioned to, and taxed by, the State, even though that dividend was taxed on an allocated, or unapportioned, basis in the foreign country and even though the foreign factors generating that dividend equalled the taxpayer's New Mexico factors. In other words, the taxpayer would be subject to tax on $300—$100 by the foreign jurisdiction and $200 by New Mexico—even though it earned only $200.

Without a doubt, New Mexico's apportionment formula should be struck down as violating *Container Corp.*'s requirement of fairness: It is internally inconsistent in that if it were applied by every jurisdiction it would result in more than 100 percent of NCR Corporation's income being taxed, and it is externally inconsistent in that it does not represent a reasonable sense of how the income was generated. *See Container Corp.*, 463 U.S. at 169-70. The Court should grant a writ of certiorari in this case to clarify that where a State seeks to apportion nondomiciliary income, the State's apportionment formula must include an appropriate portion of the taxpayer's payroll, property, and sales. Only by requiring factor representation can the Court vindicate the constitutional requirement of a "fair" apportionment formula. *Container Corp.*, 463 U.S. at 169.

II. NEW MEXICO'S TAXING SCHEME INEVITABLY LEADS TO DOUBLE TAXATION AND THEREFORE VIOLATES THE FOREIGN COMMERCE CLAUSE

The constitutional prohibition against state taxation of *foreign* commerce is "broader than the protection afforded to interstate commerce . . . ." *Kraft Gen. Foods, Inc. v. Iowa Dep't of Revenue & Finance*, 112 S. Ct. 2365, 2370 (1992) (citing *Japan Line, Ltd. v. County of Los Angeles*, 441 U.S. 434, 445-46 (1979)). Thus, a state tax cannot survive scrutiny under the Foreign Commerce Clause if the tax creates a substantial risk of international multiple taxation, or prevents "the Federal Government

from 'speak[ing] with one voice when regulating commercial relations with foreign governments.'" *Japan Line*, 441 U.S. at 451 (quoting *Michelin Tire Corp. v. Wages*, 423 U.S. 276, 285 (1976)). The elevated protection for foreign commerce—which extends not only to foreign taxpayers but to U.S. taxpayers engaged in such commerce—owes itself to the realization that a State's interference with "foreign commerce may create problems, such as the potential for international retaliation, that concern the Nation as a whole." *Kraft Gen. Foods*, 112 S. Ct. at 2370. *Amicus* TEI submits that, even if New Mexico's statute did not offend the Commerce and Due Process Clauses, it should fall under the Foreign Commerce Clause.

To prevent multiple taxation of interstate commerce, a State's apportionment formula must be applied in a manner such that "no instrumentality of commerce is subjected to more than one tax on its full value." *Japan Line*, 441 U.S. at 447. Although in the domestic context the Court may "enforce full apportionment by all potential taxing bodies," it cannot ensure full aportionment when one of the taxing authorities is a foreign nation. *Id.* In such situations, if a State's taxing scheme "inevitably" leads to multiple taxation, it must be struck down under the Foreign Commerce Clause. *Container Corp.*, 463 U.S. at 188; *Japan Line*, 441 U.S. at 447.

In this case, the State of New Mexico included in the apportionable tax base the dividends, interest, and royalties received by the taxpayer from its foreign subsidiaries —income that was subject to tax in full without apportionment by foreign taxing authorities. (App. B at 31a-33a.) Thus, one taxing jurisdiction has claimed the right to tax a given value in full, and another taxing jurisdiction has claimed the right to tax the same entity in part—"a combination resulting necessarily in double taxation." *Itel Containers Internat'l Corp. v. Huddleston*, 113 S. Ct. 1095, 1103 (1993) (quoting *Container Corp.*, 463 U.S.

at 188);[12] *accord Mobil*, 445 U.S. at 444-45 ("[t]axation by apportionment and taxation by allocation to a single situs are theoretically incommensurate . . ."). If other States were to follow New Mexico's lead (and, regrettably, many have adopted similarly flawed schemes), "various instrumentalities of commerce could be subjected to varying degrees of multiple taxation, a result that would plainly prevent this Nation from 'speak[ing] with one voice' in regulating commerce." *Japan Line*, 441 U.S. at 450-51 (quoting *Michelin Tire Corp.*, 423 U.S. at 285).[13]

Amicus TEI submits that the Foreign Commerce Clause does not permit such apportionment of foreign income without taking into account the property, payroll, and sales factors that generated the income. Requiring the

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[12] In *Itel*, the Court stated that the Foreign Commerce Clause cannot be interpreted to demand that a state refrain from taxing any business transaction that is *potentially* subject to taxation by a foreign sovereign. 113 S. Ct. at 1104. Here, in contrast, the lower court found multiple taxation to be real. (App. A at 11a.) Moreover, the tax upheld in *Itel* fell on a discrete transaction occurring within Tennessee and the State there provided a credit for any tax properly paid in another jurisdiction, foreign or domestic, on the same transaction. 113 S. Ct. at 1104. In this case, New Mexico included the taxpayer's entire foreign dividend, interest, and royalty income in the apportionment formula without providing any sort of credit.

[13] The hearing officer in this case averred that multiple taxation was not inevitable because not every foreign country in which the taxpayer operated chose to tax its dividends, interest, and royalties. (App. B at 49a-50a.) Such a facile analysis, however, misapprehends the Court's foreign commerce jurisprudence: there is no requirement that an apportionment scheme result in tax *in every instance*, only that multiple taxation—whether in one or more jurisdictions—be unavoidable. *Japan Line*, 441 U.S. at 452. As the Court found in *Japan Line*, "[e]ven a slight overlapping of tax—a problem that might be deemed *de minimis* in a domestic context—assumes importance when sensitive matters of foreign relations and national sovereignty are concerned." *Id.* at 456 (footnote omitted). Even the New Mexico Court of Appeals conceded that multiple taxation was "real." (App. A at 11a.)

States to provide factor representation is necessary to prevent the inevitable multiple taxation that would otherwise ensue.[14] In *Mobil*, the Court left open the question whether the Foreign Commerce Clause required factor representation because the issue had not been properly raised. 445 U.S. at 449. The Court should grant a writ of certiorari to redress this constitutional violation.

III. THE DECISION OF THE COURT BELOW CONFLICTS WITH THIS COURT'S DECISION IN *KRAFT GENERAL FOODS*

A writ of certiorari should issue in this case because the decision of the New Mexico Court of Appeals conflicts with this Court's 1992 decision in *Kraft General Foods*. In that case, this Court scrutinized an Iowa statute that used the federal definition of "net income" with certain adjustments. For federal tax purposes, corporations are generally allowed a deduction for dividends received from domestic subsidiaries. I.R.C. § 243 (1986). In following the federal scheme, Iowa permitted a deduction for dividends from domestic subsidiaries, but included dividends from foreign subsidiaries in taxable income. The Court found that the "State's preference for domestic commerce over foreign commerce [was] inconsistent with the Commerce Clause . . . ." 112 S. Ct. at 2370. The Court therefore held the Iowa statute unconstitutional because it "facially discriminate[d] against foreign commerce and therefore violate[d] the Foreign Commerce Clause." *Id.* at 2372.[15]

Like the Iowa statute involved in *Kraft General Foods*, the New Mexico statute here defines "net income" as fed-

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[14] The failure to provide factor representation thus distinguishes this case from *Container Corp.*, where the sustained California taxing scheme included not only the combined income, but also the combined factors of the taxpayer and its subsidiaries. 463 U.S. at 174-75.

[15] The Court also held that the flow of value, including dividends, between Kraft and its foreign subsidiaries constituted "foreign commerce." 112 S. Ct. at 2369.

eral taxable income with certain adjustments for New Mexico tax purposes. N.M. Stat. Ann. §§ 7-2A-2(C) and (I) (Michie 1978) (1993 Repl.). (App. D at 71a.) Because NCR Corporation filed returns on a federal consolidated basis (App. B at 21a), transactions between members of the domestic consolidated group (such as dividends, interest, and royalties) were effectively eliminated from NCR Corporation's apportionable base for New Mexico tax purposes.[16] Thus, under the New Mexico statute, NCR Corporation's taxable income did not generally include dividends, interest, and royalties received from domestic subsidiaries, but did include similar intercompany payments received from its foreign subsidiaries.[17] (App. B at 26a-27a.) Moreover, the factors that generated that income from the domestic subsidiaries were included in NCR Corporation's apportionable tax base, whereas the factors relating to the income from the foreign subsidiaries were not.

In *Kraft General Foods*, the Court found the dichotomy between the treatment of dividends received from domestic and foreign subsidiaries discriminatory, unjustified,

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[16] Under the applicable Treasury Regulations, dividends distributed from one member of a consolidated group to another member are eliminated in calculating taxable income. Treas. Reg. § 1.1502-14(a)(1) (1993). With respect to interest and royalties, there is essentially a "wash" between the two members of a consolidated group. Thus, if Member A makes an interest payment on an indebtedness to Member B, Member A receives a deduction for the interest and Member B is required to take the interest payment into income. Treas. Reg. § 1.1502-13(b)(1) (1993) (setting forth the rules for treatment of intercompany transactions). Because foreign subsidiaries are not generally part of the consolidated group, no member of the consolidated group may take a deduction for federal tax purposes for income payments received from foreign subsidiaries opearting abroad.

[17] The dividends, interest, and royalties NCR Corporation received from its foreign subsidiaries were also included in its federal taxable income, but the federal taxing scheme allows a credit for taxes paid to foreign taxing authorities. I.R.C. § 901 (1986); *see* App. B at 23a. New Mexico does not allow such a credit for foreign taxes.

and constitutionally fatal. *Id.* at 2372. The New Mexico statute is similarly flawed.

With respect to dividends, *Kraft General Foods* unwaveringly teaches that a statute that differentiates between the deduction for domestic dividends and the deduction for foreign dividends facially discriminates against foreign commerce. In addition, the New Mexico statute treats interest and royalties received from foreign subsidiaries differently from the payments received from domestic subsidiaries. Finally, New Mexico failed to take into account the factors generating the income for the foreign subsidiaries, while the factors for domestic subsidiaries were included in the formula. New Mexico thus "imposes a burden on foreign subsidiaries that it does not impose on domestic subsidiaries." *Kraft Gen. Foods,* 112 S. Ct. at 2371. *See also Boston Stock Exch.,* 429 U.S. at 329, where the Court unequivocally held that the Commerce Clause proscribes the granting of a preference to one form of commerce over another. This discrimination between foreign and domestic entities is "wholly inconsistent with the free trade purpose of the Commerce Clause." *See id.* at 336. This Court should grant certiorari to reject this preference.

CONCLUSION

For the foregoing reasons, the Court should grant a writ of certiorari in this case.

Respectfully submitted,

TIMOTHY J. MCCORMALLY
Counsel of Record
MARY L. FAHEY
TAX EXECUTIVES INSTITUTE, INC.
1001 Pennsylvania Ave., N.W.
Suite 320
Washington, D.C. 20004-2505
(202) 638-5601
Counsel for Amicus Curiae
Tax Executives Institute, Inc.

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